

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
ROOM 211
FEDERAL BUILDING AND U.S. POST OFFICE
225 SOUTH PIERRE STREET
PIERRE, SOUTH DAKOTA 57501-2463

IRVIN N. HOYT
BANKRUPTCY JUDGE

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January 27, 2005

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Subject: ***Robinson v. Fairbanks Capital Corporation***
(In re Gregory Antonio Robinson and Melinda Robinson)
Adv. No. 04-4045
Chapter 13; Bankr. No. 04-41154

Dear Counsel:

The matter before the Court, pursuant to the stipulation of the parties, is the issue of whether Debtors must pay Fairbanks Capital Corporation ("Fairbanks")¹ "interest on interest" to cure their default under the mortgage and promissory note held by Fairbanks. This is a core proceeding under 28 U.S.C. § 157(b)(2). This letter decision and accompanying order and judgment shall constitute the Court's findings and conclusions under Fed.R.Bankr.P. 7052. As set forth below, Debtors are required under South Dakota law to pay Fairbanks "interest on interest" to cure their default.

Summary. On May 25, 1999, Gregory A. Robinson and Melinda R. Robinson ("Debtors") executed a mortgage and promissory note in favor of EquiCredit Corporation of America ("EquiCredit"). Some time thereafter, EquiCredit transferred the mortgage and promissory note to Fairbanks.² Debtors defaulted on the mortgage and promissory note.

¹ Fairbanks Capital Corporation is the "servicer" for United States Bank National Association, f/k/a First Bank National Association Trust, acting solely in its capacity as trustee for EQCC Home Equity Loan Trust 199-3.

² The circumstances surrounding the transfer are not readily apparent from the record.

On May 17, 2004, Debtors filed a petition for relief under chapter 13 of the bankruptcy code. In their plan, which they filed on June 2, 2004, Debtors proposed to make their regular monthly payments under the mortgage and promissory note and to pay Fairbanks \$19,700, without interest, to cure their default. On July 12, 2004, Fairbanks filed an objection to Debtors' plan, in which it stated that the amount of Debtors' default was \$23,657.02.³ On August 23, 2004, Fairbanks filed an amended objection to Debtors' plan, in which it "further object[ed] to [Debtors'] effort to pay arrearages at zero percent interest."

In the meantime, on August 5, 2004, Debtors commenced the instant adversary proceeding to determine the "validity and extent" of Fairbanks' claim.⁴ Fairbanks answered Debtors' complaint on August 23, 2004. At a pre-trial conference on November 10, 2004, the parties advised the Court that they had resolved the amount of Fairbanks' claim for arrearages and that the only remaining issue was whether Fairbanks was entitled to "interest on interest."⁵

³ Fairbanks filed an earlier objection to Debtors' plan, but withdrew it on August 4, 2004.

⁴ While Debtors refer to Fed.R.Bankr.P. 7001(2) and 28 U.S.C. § 157(b)(2)(K) in the first numbered paragraph of their complaint, they did not ask the Court to determine the validity, priority, or extent of a lien or other interest in property, nor did they request any other relief of the kind specified in Fed.R.Bankr.P. 7001. Thus, Debtors did not need to commence an adversary proceeding. A simple objection to claim would have sufficed. See Fed.R.Bankr.P. 3007.

⁵ The hearing minutes for the pre-trial conference indicate the parties intended to rely on the Court's decision in *In re Andrew A. Erickson and Kitsey K. Erickson*, Bankr. No. 03-41403 (Bankr. D.S.D.), to resolve the "interest on interest" issue. In that case, by order entered September 3, 2004, the Court directed the parties, represented by the same counsel involved in this adversary proceeding, to file briefs on or before the last date to object to the debtors' second modified plan. However, neither party timely filed a brief in *Erickson*. Counsel instead conferred between themselves and "moved" the briefing of the "interest on interest" issue to this adversary proceeding. The Court generously accommodated Counsel by entering a scheduling order on December 9, 2004.

By Order dated December 3, 2004, the Court approved the parties' oral stipulation that Fairbanks would amend its proof of claim to reflect a claim of \$21,319 for arrearages and the parties would submit "the compound interest issue" to the Court on briefs.⁶ The parties submitted briefs, and the matter was taken under advisement.

Discussion. Pursuant to 11 U.S.C. § 1322(e), "if it is proposed in a plan to cure a default, the amount necessary to cure the default shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law." Thus, the Court must examine both the parties' agreement and applicable nonbankruptcy law. See *In re Young*, 310 B.R. 127, 130 (Bankr. E.D. Wis. 2003); *In re Koster*, 294 B.R. 737, 739-40 (Bankr. E.D. Mo. 2003); *In re Trabal*, 254 B.R. 99, 102 (Bankr. D.N.J. 2000).

With respect to the parties' agreement, the second numbered paragraph of the promissory note clearly provides that "[s]ubject to applicable law, the Note Holder shall be entitled to interest at the yearly rate [13.65%] on any mortgage arrearage (amount past due)" In their brief, Debtors argued that "it is certainly an ambiguous question as to what the term 'interest . . . on any [m]ortgage arrears' may actually refer to." The Court disagrees. Debtors overlooked - or disregarded - the parenthetical that immediately follows the language they chose to quote. Any "amount past due" is a "mortgage arrearage."

Pursuant to the third numbered paragraph of the promissory note, Debtors were obligated to make monthly payments of principal and interest beginning on July 1, 1999 and continuing on the first of each month thereafter until June 1, 2014. Debtors' failure to make one or more of those payments in a timely manner created an "amount past due" (or a "mortgage arrearage"). Under the mortgage and promissory note, Fairbanks is therefore entitled to interest at the yearly rate of 13.65% on each such payment that is past due, including the portion of each such payment that represents interest.

With respect to applicable nonbankruptcy law,⁷ it has long

⁶ Fairbanks does not yet appear to have amended its claim.

⁷ In their brief, Debtors argued that the Home Ownership and Equity Protection Act of 1994 ("HOEPA"), Regulation Z, and RESPA have some bearing on the issue before the Court. However,

been the rule in South Dakota that a party is entitled to interest on accrued but unpaid interest.

The objection made by the appellant's counsel, that the computation was unjust and inequitable, is sufficiently answered by reference to the contract, and the debtor could easily have avoided any injustice in this direction by complying with its terms, and paying the debt as agreed. Entertaining the view, then, that the clear, unequivocal intention of the parties to this contract was to provide for the payment of interest upon the installments of interest which should be unpaid and withheld by the appellant, we find no error in the method of computation adopted by the court below on the unpaid installments of interest which accrued previous to the time of maturity of the principal sum, after the debt became due by the terms of the contract.

Hovey v. Edmison, 22 N.W. 594, 606 (Dakota 1885) (citations therein).

"Simple interest" is straight interest computed on the principal from the time interest is to commence to the time of payment or judgment. "Compound interest" is interest added to the principal as the interest becomes due, and thereafter made to bear interest. There is another recognized form of interest. "Annual interest" is simple interest figured on each year's unpaid interest from the time it becomes due to the date of judgment and at the rate provided by the terms of the contract. These have long been recognized in our jurisdiction. In *Hovey* our Territorial Court expressly approved the annual interest computation method, terming it a middle course.

Wieland v. Loon, 116 N.W.2d 391, 393 (S.D. 1962) (citations omitted). See also *Robinson v. Cooke*, 251 N.W. 300, 304 (S.D. 1933) (citing *Hovey* for the proposition that "a promissory note providing for the payment of interest annually and stipulating that each annual installment of interest not paid when due

Debtors did not raise this argument in their complaint, choosing instead to rely exclusively on South Dakota law. The Court has therefore limited itself to a consideration of South Dakota law. If Debtors believe they have a valid claim against Fairbanks under HOEPA, Regulation Z, RESPA, or other federal laws, they may commence an appropriate proceeding.

should bear interest at a specified rate from the time it fell due until paid, was valid and legal"); *Goodale v. Wallace*, 103 N.W. 651, 653-54 (S.D. 1905) (citing *Hovey* for the proposition that "[t]he provision in contracts for the payment of a simple interest upon accrued interest on notes and obligations does not in this state constitute usury"). Debtors have not cited the Court to, and the Court has not found, any more recent authority to the contrary.

In accordance with the underlying agreement and applicable nonbankruptcy law, the Court concludes that Debtors are required to pay Fairbanks "interest on interest" to cure their default.⁸ The parties' having stipulated to the amount of Fairbanks' claim for arrearages, there are no remaining issues to be resolved in this adversary. The Court will therefore enter an appropriate order and judgment.⁹

Sincerely,

/s/ Irvin N. Hoyt

Irvin N. Hoyt
Bankruptcy Judge

INH:sh

cc: case file (docket original; serve parties in interest)

⁸ Debtors' reliance on *In re Milham*, 141 F.3d 420 (2nd Cir. 1998), and *Till v. SCS Credit Corporation*, 541 U.S. 465, 124 S.Ct. 1951 (2004), for the proposition that if Debtors must pay interest on interest, something other than the contract rate should be used is misplaced. Both *Milham* and *Till* involved the rights of a creditor whose claim was secured by personal property. In such cases, "the court's authority to modify the number, timing, or amount of the installment payments from those set forth in the debtor's original contract is perfectly clear." *Till*, 124 S.Ct. at 1959. The instant case, on the other hand, involves the rights of a creditor whose claim is secured by the debtor's principal residence. In such cases, the "anti-modification" provision of 11 U.S.C. § 1322(b)(2) operates to forbid any such modification of the secured creditor's rights. See *Rake v. Wade*, 508 U.S. 464, 468-69 (1993); *Nobelman v. American Savings Bank*, 508 U.S. 324, 327-28 (1993).

⁹ Nothing in this letter decision or the accompanying order and judgment should be taken as prohibiting Fairbanks from voluntarily agreeing to a reduction in the annual rate of interest or some other accommodation to assist Debtors in their efforts to reorganize their financial affairs.